



GOLD DĪNĀR AS ALTERNATIVE MONEY:
A HISTORICAL AND JURISTIC ANALYSIS

BY

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ABSTRACT

This study aims to examine and analyze the history of gold dīnār starting from the Prophetic era until Ottomans, proposing gold dinar as an alternative. In addition, this research gives a detailed study on economic and monetary integration among Muslim countries, nature of monetary currency, its functions and its evolution from the Islamic perspective. This study sheds light on the advantages and disadvantages of gold and fiat money and provides analysis of classical and modern scholars' view. The research relies on the analytical evocative methodology to achieve its objectives. It extracts several findings such as the differences of gold dinar weight during the Umayyad and Abbasid period, the views of classical scholars on the value of gold as a medium of exchange, measure of values and a means to possess other objects. The gold dīnār has played an important role and successfully left an immense impact on the economy in both Muslim and European countries. Furthermore, it describes the view of modern Muslim scholars where most of them accept fiat money while some prefer gold as money. However, the majority of the scholars are of the opinion that fiat money is the cause of the financial crisis in the world today. Moreover, contemporary Muslim scholars suggest implementing gold dīnār by settlement of debt and using gold as a medium of exchange through the IDB and OIC channel. Finally, this research gives some suggestions to solve the problem of inflation and bring the stability in our financial monetary system and business. This is by proposing a suitable monetary system from the Islamic jurists' perspective for the Muslim world that will be protected from financial and economic crises and free them from servitude to the West due to the use of the fiat money monetary system.

خلاصة البحث

تهدف هذه الدراسة إلى فحص وتحليل تاريخ الدينار الذهبي بدءاً من العصر النبوي حتى العصر العثماني، واقتراح الدينار الذهبي بديلاً للتبادل. كما قدمت الدراسة تفصيلاً عن التكامل الاقتصادي والنقدي بين الدول الإسلامية، وطبيعة العملة النقدية، ووظائفها وتطوراتها من منظور إسلامي. وتسلط الدراسة الضوء كذلك على مزايا وعيوب الذهب والعملية الورقية وتقديم تحليل من وجهة نظر العلماء الكلاسيكيين والمحدثين. واستخدمت الدراسة منهج التحليل الاقتراحي لتحقيق أهدافها. واستنتجت الدراسة نتائج عدة من خلال التحليلات مثل الفروق المتعلقة بوزن الدينار الذهبي خلال الفترة الأموية والعباسية، ووجهات نظر العلماء الكلاسيكيين فيما يتعلق بقيمة الذهب وسيلة للتبادل، وقياس القيم و وسيلة لامتلاك أشياء أخرى. ووصلت النتائج إلى أنّ الدينار الذهبي أدى دوراً مهماً وترك بنجاح تأثيراً كبيراً في الاقتصاد في كل من الدول الإسلامية والأوروبية على حد سواء. وعلاوة على ذلك، فإن الدراسة وصفت وجهات نظر العلماء المحدثين، حيث قبل كثيرٌ منهم استخدام العملة الورقية وفضل بعضهم الذهب نقوداً للتداول. لكن الغالبية العظمى من العلماء ذهبوا إلى أن النقود الورقية هي سبب الأزمات المالية العالمية في الوقت الحاضر. واقترح علماء المسلمين المعاصرين كذلك تطبيق نظام الدينار الذهبي عن طريق قضاء الديون، واستخدام الدينار الذهبي وسيلةً للتبادل بين البنك الإسلامي للتنمية ومنظمة التعاون الإسلامي. وأخيراً، قدمت الدراسة بعض الاقتراحات والتوصيات للتغلب على مشكلة التضخم الاقتصادي وخلق التوازن في نظام العملة النقدية والأعمال. ويمكن تحقيق هذا إذا ما تم تقديم نظام نقدي مناسب من وجهة نظر الفقهاء المسلمين للعالم الإسلامي، والذي يكون مصوناً من الأزمات الاقتصادية والمالية، وتحريرهم من العبودية الغربية التي يعود سببها إلى استخدام نظام العملة النقدية الغربية.

APPROVAL PAGE

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DECLARATION

I hereby declare that this dissertation is the result of my own investigation, except where otherwise stated. I also declare that it has not been previously or currently submitted as a whole for any other degree at IIUM or other institutions.

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To my father Haji Munir Hussain and mother Farida Bano

who raised me with care and love...

To my wife who always with me along the journey

To my children Aisha Batul, Ruqia Hussain and

Muhammad Abu Bakar

To my siblings Aziz Hussain, Kulsoom Bana,

Ghafar Husain and Hafiz Ahmad Hussain

To all of them I dedicate this work

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CHAPTER 1

INTRODUCTION

1.1 OVERVIEW OF STUDY

Human beings have been living a very simple life since time immemorial. Their living was based on only basic needs. They were at that time obtaining all their needs through their personal efforts. They wandered about for their living through hunting, eating fruits, and taking caves as home. They were not in need of exchange of materials and the use of money.

Later on human beings changed their lifestyles and they started to live in groups for they felt they needed each other for interdependency, which led to barter as a medium of exchange and trading, to acquire materials and services they needed. This is because no one can produce everything one needs. At the same time, he needed to dispose the excess of his produce in which he had knowledge. In order to achieve this purpose, human beings thought about something for measuring the value of materials or produce which would make it easier for the exchange of goods and services (Qudāmah, 2002: 175).

Hence, the introduction of barter trade as the first way to get their needs, which means exchange of commodities for one another without the use of money. As a result of the difficulties that accompanied bartering, people tried to think about other means that could facilitate their commercial dealings. They reached out to money commodities .It means people agreed among themselves to use money as a medium of exchange. Then they used it to buy any commodity they wanted. Therefore, there were different types of money used as a medium of exchange at different periods of time,

places and by different people. For instance, they used stone as a medium of exchange but were abandoned because there were a lot of stones. Then, followed by the use of animals as a medium of exchange, but they also posed problems as a result of difficulties in differentiating them or to make small exchanges. Cheap minerals, like metal and copper were also used as a medium of exchange but again faced a lot of difficulties. All these led them to make use of silver and gold as money to serve as medium of exchange.

The beginning of the use of gold coin as a medium of exchange started from the Greeks. By 546 B.C Persians invaded Greece and was annexed to Asia. This system of manufacturing money was then copied from the Greeks by the rest of Asia. Silver was therefore, used by the Persians as a substantial currency, because it was found in abundance. The Romans in 350 B.C were also influenced by the Greeks, who led them to use gold as currency and manufacture money. Furthermore, because of the Roman and Persian domination on most part of the ancient world empire, dealings with gold and silver spread all over the world and became the trustful media of exchange among people.

To buttress the above statement Shapiee and Zahid (2010 :341) opined that at the time of the Prophet Muhammad (peace be upon him), the Muslims used Byzantine Gold Dīnār, Persian silver sigloi (Vickers, 1996:172) which the Muslims called *dirham*, Himyarite coins from Yemen (but were not popular) or raw metals and other commodities as money. These specie coins were accepted on their weight and not on their face value (Zaman, 1991:341). Some of the companions of the Prophet (peace be upon him) used to practice as private moneychangers (Bukhārī, vol. 3) and they exchanged gold or silver for coins in use at moderate charges (Zaman, 1991: 342). Three sorts of metal were used for economic transactions: gold (*dīnār*), silver

(*dirham*), and copper (*fals* plural *fulūs*). However, *fulūs* were intended for small monetary transactions and they did not enjoy full juridical status (see Noonan, 1974).

The Muslim Government struck its own silver *dirham* as early as 18H, although gold and silver coins from the Byzantine and Persian empires were still accepted throughout the Islamic world. Until 72 H, Muslims' use of coinage was unorganized, irregular and most often became a personal affair of the reigning caliph (Zaman, 1991). However, Abdul Malik bin Marwān (695 AD/76 AH) changed these state of affairs by introducing a national system of monetary practice. Old Byzantine and Persian figured coins were displaced by new Islamic coins and new ideas were introduced. Government mints were set up through the Islamic world and a uniform standard for each coin was prescribed and the minting of coins was subject to governmental control and regulations (Zaman, 1991: 343). Since the exchange rate between gold and silver was stable there was no problem for the Muslims to abide by the bimetallic standard for almost 400 years. (Ehrenkreutz, 1954: 3).

Gold has played an important role in human life. Gold has desirable physical characteristics such as flexibility, durability, and immunity to tarnish. Its scarcity makes it a useful store of value (Mark Duckyenfield: 2004: 20). The history of gold as money could be traced back to 6,000 years of Ancient Egypt and the civilization of Mesopotamia. Gold has unique properties as a multicurrency investment and serves as an excellent medium for both within and across currency lines (Shermen, 1986: 30).

The fiat money is artificial money, and the Gold Dīnār is real money. The real money has intrinsic value. Real money cannot be created at the denre of one. Therefore the solution to the problem of the fiat monetary system seems to lie in commodity money, and gold is a commodity that can last. All any time and in all

nations of the world, gold is accepted as an international medium of exchange that has intrinsic value (Meera, 2004: 69).

In seventeenth century gold and silver coins circulated as the legal tender in England. But the silver was most preferred the double. In early nineteenth century, when the political and economic reform hold led to emergence the gold as a coin took the place and silver displacement as anything as subsidiary English currency. When the English civil war started so they created the bank of England in 1694 to provide a secure funding cure to finance England's war with France. But it was limited, government coupled and it was providing the social bias for England state monetary standard during the eighteenth and nineteenth century (Mark, 2004: 20).

The bank failures of the 1930s and the wave of systemic banking crises over the last 25 years both originated from a very similar chain of event. Whenever the bank broken the gold based monetary system trade imbalances facilitated credit creation and resulted in hyperinflation in asset prices and when asset price bubbles popped banks failed (Duncan, 2003: 5). The money creates through the fractional reserves requirement system and the interest changes thereupon are basically also seigniorage. In the present global monetary system developing countries lose tremendously from this seigniorage (Meera, 2004: 30). In every decades whenever the financial crises came not only western nation affected from them although Islamic countries also suffered from these crises.

In the First World War the belligerent nations in Europe terminated their promise to continue their cueing in gold as a fixed rate, despite it being the financial cornerstone of world economy since the end of Napoleonic war. During the war from 1914 to 1917, United States had been an active participant and U.S gold reserves rose 64% as Europe, exchanged its gold for American goods. But when the war ended,

gold again began to flow in the U.S and U.S allies began to repay their debts (Duncan, 2003: 18). All the money was backed by gold, until 1973, when the Bretton Woods international monetary system collapsed. Then very soon the U.S dollar replaced gold as the world's reserves currency. But it failed and got into financial crises at every decade (Duncan, 2003: 20).

1.1.1 The Evolution of the International Monetary System

This part examines the international monetary system and defines the overall financial environment in which multinational corporations and international investors operate.

The international monetary system can be defined as the institutional framework within which international payments are made, movements of capital are accommodated, and exchange rates among currencies are determined. It is a complex whole of agreements, rules, institutions, mechanisms, and policies regarding exchange rates, international payments, and the flow of capital. The international monetary system has evolved over time and will continue to do so in the future as the fundamental business and political conditions underlying the world economy continue to shift.

In this section, we will review the history of the international monetary system and contemplate its future prospects. In addition, we will compare and contrast the alternative exchange rate system that is fixed versus flexible exchange rates. For astute financial management, it is important to understand the dynamic nature of international monetary environments.

The international monetary system has gone through several distinct stages of evolution. These stages are summarized as follows:

I. Bimetallism: before 1875

2. Classical gold standard: 1875-1914
3. Interwar period: 1915-1944
4. Bretton Woods system: 1945-1972
5. Flexible exchange rate regime: since 1973

1.1.2 Bimetallism: Before 1875

Bimetallism, in economic history, is the monetary system in which two commodities, usually gold and silver, are used as a standard and coined without limit at a ratio fixed by legislation that also designates both of them as legally acceptable for all payments. The term was first used in 1869 by Enrico Cernuschi (1821–96), an Italian-French economist and a vigorous advocate of the system. In a bimetallic system, the ratio is expressed in terms of weight, e.g., 16 oz of silver equal 1 oz of gold, which is described as a ratio of 16 to 1. As the ratio is determined by law, it has no relation to the commercial value of the metals, which fluctuates constantly (Laughlin, 1895)¹.

In bimetallism, gold and silver would both be used as means of payments. The monetary unit would effectively be prescribed in gold and its prescribed equivalent in silver. If the gold and silver markets are disturbed, the relative prices of gold and silver will be altered, and it would no longer be possible. The bimetallic system itself affects in the world market of the precious metals. If the value of silver falls relatively to that of gold, the bimetallic country, offering as it does a fixed price for silver, finds itself compelled to buy unusually large quantities of it. In this case, the bimetallic country is in the position of a dealer undertaking to buy and sell unlimited quantities of both metals on fixed prices (Hawtrey, 1939:77-106).

¹ <http://encyclopedia2.thefreedictionary.com/Bimetallism>
J. L. Laughlin, *The History of Bimetallism in the United States* (1897, repr. 1968).

Prior to the 1870s, many countries had bimetallism, that is, a double standard in that free coinage that was maintained for both gold and silver. In Great Britain, for example, bimetallism was maintained until 1816 (after the conclusion of the Napoleonic Wars) when Parliament passed a law maintaining free coinage of gold but abolishing free coinage of silver. In the United States, bimetallism was adopted by the Coinage Act of 1792 and remained a legal standard until 1873 when Congress dropped the silver dollar from the list of coins to be minted. France, on the other hand, introduced and maintained its bimetallism after the French Revolution to 1878. Other countries such as China, India, Germany, and Holland were on the silver standard (S.Eun, 2009: 26).

The international monetary system before the 1870s can be characterized as "bimet-allism" in the sense that both gold and silver were used as international means of payment and the exchange rates among currencies were determined by either their gold or silver contents. For example, the exchange rate between the British pound, which was fully on a gold standard, and the French franc, which was officially on a bimetallic standard, was determined by the gold content of the two currencies. On the other hand, the exchange rate between the franc and the German mark, which was on a silver standard, was determined by the silver content of the currencies.

It is also worth noting that, due to various wars and political upheavals, some major countries such as the United States, Russia, and Austria-Hungary had irredeemable currencies at one time or another during the period 1848-1879. One might say that the international monetary system was less than fully systematic up until the 1870s. Countries that were on the bimetallic standard often experienced the well-known phenomenon referred to as Gresham's law. Since the exchange ratio between the two metals was officially fixed, only the abundant metal was used as

money, driving more scarce metal out of circulation. The United States adopted the gold standard in 1879, Russia and Japan in 1897 (Eun & Resnick, 2009: 26).

1.1.3 Classical Gold Standard: 1875-1914.

Around 1850, gold discoveries in Australia and California revolutionized the markets in the precious metals. The French franc from a silver unit became gold unit. In 1871 Russia, Austria-Hungary, Italy and the United States were using depreciated paper. Throughout Europe only in Germany, Holland and Scandinavia was the silver standard maintained. The period from 1848 to 1871 was one of wars and revolution, and the result was to drive many important countries into using paper money (Hawtrey, 1939:86).

British pound becomes reserve currency on 22nd June 1816 when Great Britain declared the gold currency as its official national currency (Lord Liverpool's Act). On 1st May 1821, the convertibility of pound sterling into gold was legally guaranteed. Other countries pegged their currencies to the British pound, which made it a reserve currency. This happened while the British continued to dominate international finance and trade relations. At the end of the 19th century, the pound was used for two thirds of world trade and most foreign exchange reserves were held in this currency.²

The international gold standard existed as a historical reality during the period 1875-1914. The majority of countries got off gold in 1914 when World War I broke out. The classical gold standard as an international monetary system thus lasted for about 40 years. During this period, London became the center of the international

² 1-http://en.wikipedia.org/wiki/Gold_standard

financial system, reflecting Britain's advanced economy and its preeminent position in international trade. (Eun & Resnick, 2009: 27)

Recent evidence suggests that, indeed, exchange rates throughout the 1880-1914 periods were characterized by a high degree of fixity in the principal countries. Although exchange rates frequently deviated from par, violations of the gold points were rare (Officer, 1986).

An international gold standard can be said to exist when, in most major countries, (1) gold alone is assured of unrestricted coinage, (2) there is a two-way convertibility between gold and national currencies at a stable ratio, and (3) gold may be freely exported or imported. In order to support unrestricted convertibility into gold, banknotes need to be backed by a gold reserve of a minimum stated ratio. In addition, the domestic money stock should rise and fall as gold flows in and out of the country. These conditions were roughly met between 1875 and 1914.

Under the gold standard, international imbalances of payment will also be corrected automatically. Consider a situation where Great Britain exported more to France than the former imported from the latter. This kind of trade imbalance will not persist under the gold standard. Net export from Great Britain to France will be accompanied by a net flow of gold in the opposite direction. This flow of gold will lead to a lower price level in France and, at the same time, a higher price level in Great Britain. The resultant change in the relative price level, in turn, will slow exports from Great Britain and encourage exports from France. As a result, the initial net export from Great Britain will eventually disappear.

The gold standard, however, has a few key shortcomings. First of all, the supply of newly minted gold is so restricted that the growth of world trade and investment can be seriously hampered for the lack of sufficient monetary reserves.

The world economy can face deflationary pressures. Furthermore whenever the government finds it politically necessary to pursue national objectives that are inconsistent with maintaining the gold standard, it can abandon the gold standard. For such reasons, it is not very likely that the classical gold standard will be restored in the foreseeable future.

1.1.4 Interwar Period: 1915-1944

World War I ended the classical gold standard in August 1914, as major countries such as Great Britain, France, Germany, and Russia suspended redemption of banknotes in gold and imposed embargoes on gold exports. After the war, many countries, especially Germany, Austria, Hungary, Poland, and Russia suffered hyperinflation.

The United States, which replaced Great Britain as the dominant financial power, spearheaded efforts to restore the gold standard. With only mild inflation, the United States was able to lift restrictions on gold exports and return to a gold standard in 1919. In Great Britain, Winston Churchill, the Chancellor of the Exchequer, played a key role in restoring the gold standard in 1925. Besides Great Britain, countries such as Switzerland, France, and the Scandinavian countries restored the gold standard by 1928.

The international gold standard of the late 1920s, however, was not much more than a facade. Most major countries gave priority to the stabilization of domestic economies and systematically followed a policy of sterilization of gold by matching inflows and outflows of gold respectively with reductions and increases in domestic money and credit.